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MEMORANDUM

TO: Docket Control Center

FROM: Steven M. Olea
Director
Utilities Division

DATE: September 22, 2010

RE: IN THE MATTER OF PROPOSED RULEMAKING ON GAS ENERGY
EFFICIENCY (DOCKET NO. RG-00000B-09-0428)

Attached is the Economic, Small Business, and Consumer Impact Statement that addresses the economic impacts of the proposed Gas Utility Energy Efficiency rules, filed in compliance with Decision No. 71855.

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ORIGINATOR: Julie McNeely-Kirwan

Arizona Corporation Commission
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Docket No. RG-00000B-09-0428

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B. Economic, Small Business and Consumer Impact Statement

1. Identification of the proposed rule making.

The rules are new Sections under Title 14, Chapter 2 - Corporation Commission, Fixed Utilities. Rules R14-2-2501 through R14-2-2520 require affected utilities, by December 31, 2020, to achieve cumulative annual energy savings, expressed as therms or therm equivalents, equal to at least 6 percent of the affected utility's retail gas energy sales for calendar year 2019.

The purpose of Gas Utility Energy Efficiency Standards is for affected utilities to achieve therm or therm equivalent savings through demand-side management ("DSM") and renewable energy resource technology application ("RET") programs in order to ensure reliable gas service at reasonable rates and costs. Energy efficiency means the production or delivery of an equivalent level and quality of end-use gas service using less energy, or the conservation of energy by end-use customers. DSM programs promote materials, devices, technologies, educational programs, practices or facility alterations designed to result in increased energy efficiency, including combined heat and power used to displace space heating, water heating or another load. RET programs promote technology applications that utilize an energy resource that is replaced rapidly by a natural, ongoing process, and that displaces conventional energy resources.

Requiring affected utilities to achieve energy savings through DSM and RET programs is an essential part of the Commission's efforts to meet its constitutional obligation to "prescribe just and reasonable rates and charges to be made and collected ... by public service corporations within the State for service rendered therein" because the amount of gas consumed by an affected utility's customers, and the pattern of usage by those customers, directly impacts the physical assets that an affected utility must have in place and the amount of pipeline capacity it must reserve, as well as the affected utility's operating expenses. Decreasing the overall consumption of energy can reduce gas costs, infrastructure costs, and distribution costs, and, in addition, reduce adverse environmental impacts (such as air emissions).

Energy efficiency is a reliable energy resource that costs less than other resources for meeting the energy needs of utility ratepayers. Increasing energy efficiency to meet the Energy Efficiency Standard set forth in the Gas Utility Energy Efficiency Standards rules will reduce the total cost of energy for affected utilities' ratepayers. Increasing energy efficiency will result in less air pollution, reduced carbon emissions, and fewer other adverse environmental impacts than would occur if energy efficiency is not increased. Increasing energy efficiency will reduce affected utilities' costs of compliance with current and future environmental regulations. Increasing energy efficiency will diversify energy

resources, reduce the overall cost of reserving pipeline capacity, and reduce the need for additional infrastructure to distribute gas.

The Rules apply to affected utilities, as defined in the Rules. The public service corporations to whom the proposed Gas Utility Energy Efficiency Standards rules currently apply, because they are affected utilities classified as Class A under A.A.C. R14-2-103(A)(3)(q), are Southwest Gas Corporation, UNS Gas, Inc., and SemStream Arizona Propane (Payson Division). None of these entities is a small business under A.R.S. § 41-1001.

2. *Persons who will be directly affected by, bear the costs of, or directly benefit from the proposed rule making.*

- a. the public at large;
- b. consumers of gas service in Arizona;
- c. gas public service corporations;
- d. Arizona Corporation Commission;
- e. manufacturers, distributors, and installers of DSM measures;
- f. manufacturers, distributors, and installers of RET equipment; and
- g. public entities, such as schools, cities, counties, and state agencies.

3. *Cost-benefit analysis.*

- a. Probable costs and benefits to the implementing agency and other agencies directly affected by the implementation and enforcement of the proposed rule making.

Probable costs to the Commission of the proposed rule making would include costs associated with reviewing filings, and participating in meetings and hearings.

To the extent that the implementing agency and other agencies are customers of affected utilities and install DSM measures or RET equipment, probable costs will include initial costs for the measures or equipment. Benefits will include lower utility bills than without these rules.

- b. Probable costs and benefits to a political subdivision of this state directly affected by the implementation and enforcement of the proposed rule making.

To the extent that political subdivisions are customers of affected utilities and install DSM measures or RET equipment, probable costs will include initial costs for the measures or equipment. Benefits will include lower

utility bills than without these rules. Political subdivisions may also benefit by increased sales tax revenues resulting from sales of DSM and RET products.

- c. Probable costs and benefits to businesses directly affected by the proposed rule making, including any anticipated effect on the revenues or payroll expenditures of employers who are subject to the proposed rule making.

Affected utilities may incur additional costs of complying with program development, program implementation, and reporting activities. Although some of the affected utilities are now engaging in some of the required activities, they may incur additional costs of complying with the rules. Payroll expenditures of affected utilities may be increased. These costs may be recovered through the affected utilities' rates to customers. Other costs may include penalties that may be imposed for failing to comply with the rules. Revenues of affected utilities may be reduced temporarily. Affected utilities will benefit from reduced costs for transporting and procuring gas.

Arizona currently has a monopoly market structure for gas utilities. The Commission generally sets rates for the gas utilities using the following formula: $(\text{Rate Base} \times \text{Rate of Return}) + \text{Expenses} = \text{Revenue Requirement}$. "Rate Base" is the dollar value of the physical assets prudently acquired and used and useful in the provision of utility service. "Rate of Return" is the authorized return on the utility's rate base and is expressed as a percentage. "Expenses" are the reasonable and prudent costs of service that cannot be capitalized, such as purchased power costs, fuel costs, salaries, and taxes. The resulting "Revenue Requirement" is the amount that a utility is authorized to collect from its customers through its rates and that the rates adopted by the Commission are designed to produce. Thus, the rates that a utility is authorized to charge its customers are inextricably related to the amount of physical assets (such as pipelines) used by the utility and the costs of service incurred by the utility (such as costs related to distribution).

The proposed Gas Utility Energy Efficiency Standards rules will impact an affected utility's revenues, at least in the interim period before the affected utility's next rate case, because DSM and RET programs may reduce therm consumption. Currently, affected utilities' rate schemes rely heavily upon volumetric rates, meaning that the amount a customer is billed by the affected utility is based in large part upon the number of therms consumed by the customer during the billing period. If that amount is reduced by the customer's decreased consumption resulting from DSM and RET programs, the affected utility's revenues will be

impacted accordingly. Rule R14-2-2511 requires that this impact be reviewed and addressed in an affected utility's rate case, if the affected utility requests to have it addressed and provides adequate documentation/records supporting its request.

If an affected utility is permitted to recover the costs of compliance with the proposed Gas Utility Energy Efficiency Standards rules through ratemaking (because the costs of compliance are included as reasonable and prudent expenses and are consistent with the requirements imposed under R14-2-2510(A)), the affected utility's revenue requirement will be impacted. Likewise, if an affected utility is permitted to recover its fixed costs and/or its net lost income/revenue resulting from Commission-approved DSM and RET programs (as contemplated under R14-2-2511), the affected utility's revenue requirement will be impacted. When an affected utility's revenue requirement is impacted, the rates charged to its customers are also impacted.

4. *Probable impact on private and public employment in businesses, agencies, and political subdivisions of this state directly affected by the proposed rule making.*

The Commission and affected utilities may need additional employees or contractors. Manufacturers, distributors, and installers of energy efficiency measures may add employees. No impact on employment in political subdivisions is expected.

5. *Probable impact of the proposed rule making on small businesses.*

- a. Identification of the small businesses subject to the proposed rule making.

To the extent that small businesses are customers of affected utilities and install DSM measures or RET equipment, probable costs will include initial costs for the measures. Benefits will include lower utility bills than without these rules.

Only public service corporations that have annual operating revenue exceeding \$5,000,000 (Class A gas utilities) will be required to comply with the rules. These entities are not small businesses.

- b. Administrative and other costs required for compliance with the proposed rule making.

None.

- c. A description of the methods that the agency may use to reduce the impact on small businesses.

Not applicable.

- d. Probable cost and benefit to private persons and consumers who are directly affected by the proposed rule making.

The public at large will benefit from increased energy efficiency because energy efficiency reduces the need for gas and the infrastructure needed to deliver it. This results in fewer adverse environmental impacts than transporting, distributing, and using gas.

The reduction in overall energy consumption that will result from the rules should result in long-term cost savings to the affected utilities and thus to their customers because of decreased demand for gas and gas transportation. In addition, the reduction in overall energy consumption will result in decreased adverse environmental impacts, such as air emissions, which should result in benefits to the public at large that cannot be adequately quantified at this time.

6. *Probable effect on state revenues.*

There may be an increase in state revenues from sales taxes on DSM and RET products. However, there may be a decrease in revenues from sales taxes on gas bills as customers reduce their consumption. There may also be increases in income taxes resulting from revenue increases of Arizona manufacturers, distributors, and installers of DSM measures and RET equipment.

7. *Less intrusive or less costly alternative methods of achieving the purpose of the proposed rule making.*

The Commission is unaware of any alternative methods of achieving the purpose of the rule making that would be less intrusive or less costly.

8. *If for any reason adequate data are not reasonably available to comply with the requirements of subsection B of this section, the agency shall explain the limitations of the data and the methods that were employed in the attempt to obtain the data and shall characterize the probable impacts in qualitative terms.*

The data used to compile the information set forth in subsection B are reasonably adequate for these purposes.